

**Joint Legislative Study  
Committee on State  
Employee Compensation**

***2002 Annual Report***

December 2002

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**Joint Legislative Study Committee  
On  
State Employee Compensation**

**2002  
ANNUAL REPORT**

**MEMBERS:**

Senator Edward Cirillo, Cochair  
Senator Marsha Arzberger  
Senator David Peterson  
William Bell  
Sandra Williams  
Shawn Nau  
Linda Strock  
Carl Williams  
Alan Maguire

Representative Debra Brimhall, Cochair  
Representative Marian McClure  
Representative Victor Soltero  
Secretary of State Betsy Bayless  
Leigh Cheatham  
Cathy McGonigle  
Kathy Peckardt  
Pam Tenney

**JOINT LEGISLATIVE STUDY COMMITTEE  
ON  
STATE EMPLOYEE COMPENSATION**

**MEMBERS:**

Senator Edward Cirillo, Cochair  
Senator Marsha Arzberger  
Senator David Peterson  
William Bell  
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Cathy McGonigle  
Kathy Peckardt  
Pam Tenney

**MEMBERSHIP:**

- Three members of the House of Representatives, not more than two from the same political party and one designated as Co-Chair, appointed by the Speaker of the House of Representatives
- Three members of the Senate, not more than two from the same political party and one designated as Co-Chair, appointed by the President of the Senate
- One member who is an employee of the State and a member of an employee association, appointed by the Governor
- Two members who are experts on employee compensation, appointed by the Governor
- Three members who are State agency directors, deputy directors or assistant directors, appointed by the Governor
- One member from the university personnel system, appointed by the Executive Director of the Board of Regents
- One member who is an expert on employee compensation, appointed by the Speaker of the House of Representatives
- One member who is an employee of the State and who has at least ten years of State service, appointed by the President of the Senate:
- Two members who are employees of the State and have at least ten years of State service, appointed by the Governor:
- One member who is an employee of this State and who has at least ten years of State service, appointed by the Speaker of the House of Representatives

**ESTABLISHMENT:**

The Joint Legislative Study Committee on State Employee Compensation was created by Laws 1998, First Special Session, Chapter 3.

## **COMMITTEE CHARGE:**

The purpose of the Committee is to: (1) study the various State personnel systems, State employee compensation and related issues, including salary, benefits, employee turnover, and comparisons to other comparable public and private employers; (2) review all payroll deductions made from State employee salaries pursuant to A.R.S. 36-612; and (3) consider issues concerning State employee medical and dental insurance coverage, including issues relating to the size of the risk pool and the type of coverage provided to State employees.

## **TERMINATION:**

December 31, 2003

## **PUBLIC MEETINGS:**

The Committee met on March 15, 2002 for presentations on the status of self-insurance and uncovered vs. covered positions. The Committee also received an update on the State's compensation ranking and market comparison.

The Committee met again on November 20, 2002 for a presentation on the State's compensation ranking and market comparison and an update on the status of self-insurance.

## **REPORT:**

The Committee is required to submit, on or before December 1 of each year, written recommendations on a long-term strategy for addressing State employee compensation.

## **COMMITTEE RECOMMENDATIONS:**

The 2002 Committee recommendations are based on a presentation by the Arizona Department of Administration and the Arizona Board of Regents at the November 20<sup>th</sup> meeting. The following is a summary of that presentation:

### **Market Comparison**

- The Joint Governmental Salary Survey (JGSS) shows the market exceeds State employee salaries by 16.4 percent (up from 13.2 percent two years ago)
- The market exceeds State employee salaries in western states by 26.3 percent (up from 15.8 percent two years ago)

### **State Employee Salary Comparison**

- The average State employee salary is behind all Arizona benchmarks in 2002
  - The average JGSS salary is approximately \$37,000
  - The average civilian salary in Arizona is approximately \$35,000
  - The average worker salary in Arizona is approximately \$34,000
  - The average State employee salary is \$32,000

### Key Indicators

- Turnover of State employees with less than two years of service was 62 percent
- Nearly half of State employees have less than four years of service
- It takes an average of ten years of service to reach midpoint
- Eleven agencies experienced reductions of more than five percent
- Excluding the Department of Economic Security and Arizona Health Care Cost Containment System, overall the State experienced a reduction of nearly three percent
- Arizona ranks 43<sup>rd</sup> in the nation in the ratio of state employees compared to overall state population
- Arizona program expenditures have increased 42 percent since 1993, while employee salaries have increased 26 percent in the same period
- Arizona ranks 47<sup>th</sup> in the ratio of total state payroll compared to overall state population

### State Employee Salary Recommendations

- Make Salary Market Adjustments to within five percent of market, including salary and benefits
- Annual adjustments to base salary
  - Mid-point or market adjustments semantic
  - Performance or merit increases
- Lump sum cash payments for exceptional performers at maximum

Three cost models have been prepared to estimate the funding necessary to achieve the State's compensation program objective of being within five percent of the overall market salary rates.

#### Model 1

Based on the 1998 five-year goal of reaching 95 percent market parity for State employee salaries, it would cost \$172,950,000 to achieve the target.

#### Model 2

This model is based on a five-year implementation strategy at 5.4 percent per year beginning in FY 2004.

FY 2004	\$70,220,720
FY 2005	\$74,012,639
FY 2006	\$78,009,322
FY 2007	\$82,221,804
FY 2008	\$86,661,804
Total	\$391,126,310

#### Model 3

This approach reduces the initial funding amount by incrementally increasing the funding requirements over a five-year period. This model is based on the presumption that at the end of the five-year period the State's revenue stream will be more favorable.

FY 2004	\$26,007,674
FY 2005	\$46,423,698
FY 2006	\$75,504,825
FY 2007	\$108,623,993
FY 2008	\$147,909,670
Total	\$404,469,860

Additionally, the Arizona Board of Regents presented information contained in the annual personnel report for the Arizona university system. The following are the projected unmet salary needs for the university system as of the end of FY 2004:

UNIVERSITY SYSTEM	UNMET SALARY NEEDS
ASU MAIN	\$52,169,400
ASU WEST	\$6,723,800
ASU EAST	\$2,285,700
NAU	\$31,027,700
UA MAIN	\$54,659,600
UA HEALTH SCIENCES CENTER	\$10,351,000
ABOR Central Office	\$181,500
SYSTEM TOTAL	\$157,398,700

#### Arizona University Salary Recommendations

- Make Salary Market Adjustments to within five percent of market, including salary and benefits

**ATTACHMENT A**



**Arizona Department of  
Administration**

**Joint Legislative Study Committee  
on State Employee Compensation**

**Status of Self-Insurance**

**Steven P. Schramm**

**March 15, 2002**

**WILLIAM M.  
MERCER**



*Department of  
Administration*

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## **Background on Self-Insurance**

- **Self-Insured — Large Employers that can Spread Risk**
  - Employer Assumes Financial Risk
  - Employer Maintains Reserves and Retains Interest
  
- **Self-Insured — Key Advantages**
  - Employer Eliminates Insurance Profit, Premium Tax and Risk Charges
  - Control of Plan Design and Flexibility Stays w/ Employer
  
- **Self-Insured — Key Disadvantages**
  - New Legal Liability Issues for State
  - Monthly Cash Flow can Fluctuate



# **Successful Health Care Contracting: Payment Must Equal Risk**

## Major Determinants of Risk

- Program Design\* — Administration
- Target Population — Enrollees
- Benefits — Covered Services/Copayments or Co-insurance
- Service Delivery Network — Type of Network

*\*Self-insurance focuses on the funding aspect of program design, but can have a ripple effect in the other areas.*



## **S If-Insuring of Health Benefits: Sample Questions to be Answered**

*Successful* Implementation will Require 18 – 24 months  
from Official Decision Date.

### **Program Design**

- Does the State want to be Fully At Risk? (Stop Loss/  
Reinsurance, Individual v. Aggregate)
- What Roles Should the State Assume? (Plan Design,  
Benefit Decisions, Vendor Selection, Appeals Process,  
Medical Management, Formulary Determination, etc.)



## **S If-Insuring of Health Ben fits: Sample Questions to be Answered**

### Target Population

- Include/Exclude Others? (ASRS)

### Benefits

- Self-Insure all Medical Options? (PPO/POS/HMO)
- Self-Insure other Benefits? (Dental/Vision)

### Service Delivery Network

- Use the AHCCCS Network?
- Continue with CIGNA Network?

# Self-Insuring of Health Benefits: Challenges



## Logistics: Operational Time Line

- Task Force to Develop Program Recommendations (4 – 6 months)
- Finalize Program Design (6 – 9 months)
- Internal Infrastructure (concurrent via Legislative/ADOA)
- Procurement Process (3 – 4 months)
- Implementation/Open Enrollment (4 – 6 months)
- Communication with State Employees (concurrent)

# **Self-insuring of Health Benefits: Challenges**



## **Practical: Functional Roles**

- **Funding**
  - Risk Management (Stop Loss)
  - Financing (Reserves/Surpluses/Interest)
  - Banking Arrangements (Funding Claim Payments)
  
- **Monitoring — Make v. Buy**
  - Quality of Care (Formulary)
  - Access to Care (Network Management, Grievance/Appeals)
  - Medical Management (Utilization Review/Disease Management)
  
- **Administration — Make v. Buy**
  - Infrastructure (Claims/Fee Schedules/Contracting)

# Question and Answer

**ATTACHMENT B**



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**ANNUAL**

**PERSONNEL REPORT**

**FOR THE**

**ARIZONA UNIVERSITY SYSTEM**

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**OCTOBER, 2002**



*Board Members*

**Jack B. Jewett**  
Tucson  
President

**Fred T. Boice**  
Tucson

**Robert B. Bulla**  
Scottsdale

**Chris Herstam**  
Phoenix

**Kay McKay**  
Flagstaff

**Christina Palacios**  
Tucson

**Gary Stuart**  
Phoenix

**Donald J. Ulrich, Jr.**  
Paradise Valley

*Student Regents*  
**Matthew Meaker**  
UA

**Danelle Peterson-Kelling**  
ASU

**Jane Dee Hull**  
Governor of Arizona

**Jaime A. Molera**  
Superintendent of  
Public Instruction

*Executive Director*  
**Linda J. Blessing, Ph.D.**

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October 4, 2002

The Honorable Jane Dee Hull, Governor of Arizona  
The Honorable Randall Gnant, President, Arizona State Senate  
The Honorable Jim Weiers, Speaker of the House of Representatives  
1700 West Washington  
Phoenix, AZ 85007

Re: Annual Personnel Report for the Arizona University System

Dear Governor Hull, President Gnant and Speaker Weiers:

On behalf of Arizona's public universities and in accordance with A.R.S. 41-763.01, the Arizona Board of Regents submits its Annual Personnel Report. The Board authorized our submission of the Annual Personnel Report at its September 27<sup>th</sup> Board meeting.

Again this year, we have provided information about salaries, turnover, faculty retention, and overtime expenditures in the university system. As the report reflects, faculty and staff salaries continue to substantially lag behind the market and, by the end of FY 2004, we project an unmet salary need of approximately \$157.4 million.

It is unfortunate that the university system's salary needs are presented this year against the backdrop of a struggling economy and a serious revenue shortfall. Pay increases sorely are needed, and we very much would like to receive sufficient funding to satisfy the unmet salary need.

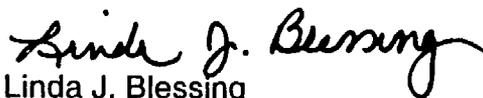
However, we also are fully cognizant of the seriousness of the current budget situation and the likelihood of further cutbacks. Consequently, we are hopeful that the revenue picture soon will improve so that the competitiveness of employee salaries can be addressed. Our public universities substantially contribute to the vibrancy of the State's economy. To preserve their strength, it

The Honorable Jane Dee Hull  
The Honorable Randall Gnant  
The Honorable Jim Weiers  
Page Two  
October 4, 2002

is essential for the universities to be able to recruit and retain talented faculty and staff, and our success in doing so is dependent upon our capacity to offer competitive salaries.

Thank you for your support of higher education.

Sincerely,



Linda J. Blessing  
Executive Director

Enclosures

c: Regent Jack Jewett  
President Michael Crow  
President John Haeger  
President Peter Likins

**ANNUAL PERSONNEL REPORT  
TO THE GOVERNOR AND THE LEGISLATURE  
FOR THE ARIZONA UNIVERSITY SYSTEM  
OCTOBER, 2002**

**BACKGROUND**

A.R.S 41-763.01 requires the Arizona Board of Regents (ABOR) annually to submit a report on university personnel to the Governor and the Legislature.

Accordingly, each university annually reviews and compares its employees' salaries with those salaries offered at peer institutions and in other relevant labor markets. Using this information, ABOR prepares and submits the required system-wide report.

In November 1996, the Board adopted a three-year plan to Restore Competitiveness to University Salaries, which was the basis for the University System's salary requests in the ensuing years. The plan was designed to raise the average salaries of employees to the 50<sup>th</sup> percentile/market average.

In 1997, a Joint Legislative Study Committee was established and charged with the responsibility of recommending long-term strategies to the Governor and legislative leadership for addressing State employee compensation. The *stated legislative goal* was to become competitive with the market by the end of FY 2003. In November 1998, ABOR presented to the Joint Committee its updated multi-year salary plan to achieve market competitiveness for the University System.

The salary adjustments authorized by the legislature for FY 1998 through FY 2003 are delineated on the next page. For these six fiscal years, the approved funding for salary increases has been much less than that required to raise university salaries to the 50<sup>th</sup> percentile/market average. When the Board adopted its 1996 plan to restore competitive salaries, university salaries already were well behind the market. The subsequent salary adjustments granted by the legislature have not been sufficient either to catch up with the market or to keep pace with upward salary movement in the relative labor markets since 1996.

**SALARY ADJUSTMENTS AUTHORIZED BY THE LEGISLATURE  
FOR FY 1998 THROUGH FY 2003**

<b>FY 1998</b>	<b>2.5% across-the-board increase up to a maximum of \$1,000 plus 2.5% merit increase pool</b>
<b>FY 1999</b>	<b>2.5% merit increase pool</b>
<b>FY 2000</b>	<b>2% merit increase pool</b>
<b>FY 2001</b>	<b>2% merit increase pool</b>
<b>FY 2002</b>	<b>\$1,450 per FTE across-the-board increase*</b>
<b>FY 2003</b>	<b>\$0*</b>

**\*The greater of 5% or \$1,500 initially was authorized and later rescinded.**

To stem the ever-widening gap, the universities reallocated funds, reduced programs and left positions vacant to generate additional salary funds. In spite of the universities' efforts to increase salaries with alternative funding, employee salaries still significantly trail that of their peers and other relevant markets. These gaps continue to increase as competing markets provided larger annual salary adjustments.

For FY 02 and FY 03, ABOR requested \$139 million for salary adjustments to enable the universities to catch-up and keep-up with their markets. Further, the Board requested an additional \$20 million for special market adjustments to address the universities' most critical salary issues.

Although the legislature did not fund ABOR's request for these fiscal years, it initially did provide funding for salary adjustments amounting to the greater of five percent or \$1,500 per FTE. However, due to the State's budget situation, the legislature later rescinded these increases, authorizing instead a \$1,450 per FTE across-the-board increase effective June 8, 2002, with no funding for salary adjustments in FY 03.

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# MARKET COMPARISONS

## METHODOLOGY

Each university and the ABOR central office compared faculty and staff salaries against salaries at peer institutions and in other relevant labor markets. The universities used the latest data (Fall 2001) from the American Association of University Professors (AAUP) to compare average faculty salaries with those of the ABOR-approved peer institutions and other comparator organizations. They also used the most recent, relevant, and available data to compare salaries for all other employee groups.

When direct comparative compensation data were available, the universities calculated the difference between average market salaries and average university salaries. For jobs without such comparative data, the universities calculated the same distance from market as for similar employee categories.

The salary surveys used in the calculations include:

- American Association of University Professors (AAUP)
- Association of American Medical Colleges
- Association of American Universities Data Exchange
- Council on Teaching Hospitals Housestaff Stipends
- Association of Research Libraries
- Joint Governmental Salary Survey (JGSS)
- College and University Personnel Association (CUPA)
- State Higher Education Executive Officers (SHEEO) Staffing and Salary Survey
- Other local and job-specific survey data.

In calculating salary needs, the universities determined the amount required to raise average faculty salaries to the 50<sup>th</sup> percentile (median) of their peers' faculty salaries and to raise other staff salaries to the average or median of their respective markets.

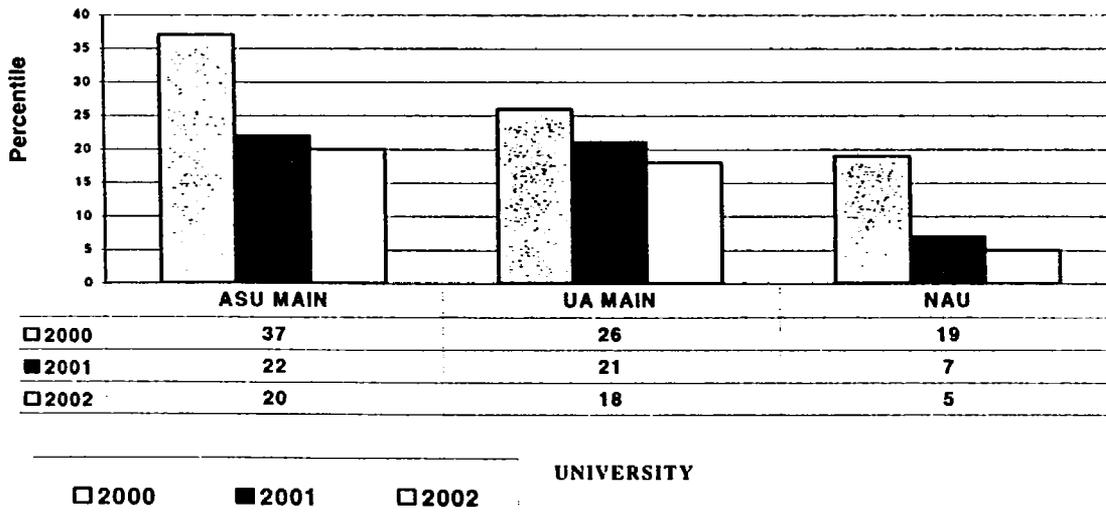
## FACULTY SALARIES

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Arizona's universities compete with hundreds of other universities throughout the country to attract and retain talented faculty. The competitiveness of salaries is quite often the single most important factor in determining whether an individual hires on or stays with Arizona's public universities. To assess how competitive Arizona's salaries are compared to the national marketplace, the universities calculate percentile rankings, comparing faculty salaries in Arizona to those in peer institutions and other comparator public universities. These comparisons include all ranked faculty made up of professors, associate professors, and assistant professors.

The faculty percentile ranking for ASU Main, UA Main, and NAU for three years are reflected in the chart below.<sup>1</sup> For all three universities, the percentile rankings have declined. Specifically, ASU Main's percentile ranking dropped from 37<sup>th</sup> to 20<sup>th</sup>; UA Main's dropped from 26<sup>th</sup> to 18<sup>th</sup>; and NAU's dropped from 19<sup>th</sup> to 5<sup>th</sup>. Although not reflected on the chart, the percentile ranking for ASU West declined over these same years from 26<sup>th</sup> to 9<sup>th</sup>. The peer/comparator universities are listed in Exhibit 1 at the end of this report.

PERCENTILE RANKINGS  
FY 2000 - 2002



<sup>1</sup> For consistency and comparative purposes, the percentile rankings for 2000 were recalculated with the methodology used in 2001 and 2002, which adjusted for differences in faculty makeup at the peer/comparator universities.

The FY 2002 percentile rankings clearly demonstrate that the large majority of these other universities pay higher average salaries to their faculty than each of Arizona's universities, illustrating that Arizona's standing is not competitive. Specifically, of the universities to which Arizona's universities compare salaries:

- 20 of the 28 universities pay higher average salaries than **ASU Main and UA Main**,
- 15 of the 17 pay higher average salaries than **NAU**, and
- the average salaries are as much as 26%, 27%, and 38% higher than ASU, UA, and NAU, respectively.

In addition to salary information, the annual AAUP survey also provides information regarding the value of faculty benefits. This enables comparisons of total compensation, i.e., the combined value of salary and benefits, and provides additional insight into the competitiveness of the University System.

When total compensation is calculated, the percentile rankings for ASU and UA drop significantly, and the percentile ranking for NAU increases slightly. Specifically, ASU Main drops to the 7<sup>th</sup> percentile while ASU West drops to the 1<sup>st</sup> percentile. UA Main's ranking drops to the 7<sup>th</sup> percentile, and NAU's increases to the 9<sup>th</sup> percentile.

Whether looking at average salaries or total compensation (salary plus benefits), the three universities are not positioned to compete for faculty in the national arena. Moreover, the universities are not adequately equipped to induce or retain those educators, researchers, and scientists who are foremost in their field. Such individuals, who are able to offer so much and raise the quality and stature of the universities' programs, can command top dollar. Accordingly, Arizona's public universities also need to have the capacity to meet these scholars' salary requirements and pay beyond the 50<sup>th</sup> percentile to attract and retain them.

## STAFF SALARIES

Much like faculty salaries, average staff salaries also substantially lag behind the market, and salary increases for these employees have been insufficient to catch up and keep pace with the market.

The salary adjustments initially approved for FY 02 and FY 03 would have resulted in a very positive and material gain for staff, especially for employees at the lowest salary levels who annually earn below \$30,000. These employees would have received a minimum annual increase of \$1,500, thereby increasing their base salary by more than 5% during each of these two years.

Unfortunately, the rescission of these salary increases and the substitution of a \$1,450 across-the-board increase for one year only forestalled any significant headway. For many staff members, the \$1,450 salary adjustment did little to enhance their situation since it largely was offset by the increased health insurance costs borne by employees the previous October. In October 2001, due to rising medical costs, the State's new group health insurance contract resulted in substantially higher premiums and increased co-pays for many State employees.

The table below reflects the percentage that average staff salaries would need to increase to reach the market at each university and the central office of ABOR.

### CLASSIFIED AND OTHER STAFF % TO MARKET

<u>UNIVERSITY/ABOR</u>	<u>CLASSIFIED STAFF</u>	<u>ALL OTHERS</u>
ASU MAIN	10.9%	10.7%
ASU WEST	13.9%	13.1%
ASU EAST	10.9%	10.7%
NAU	13.5%	8.4%
UA	15.7%	13.3%
ABOR Central Office	3.3%	10.1%

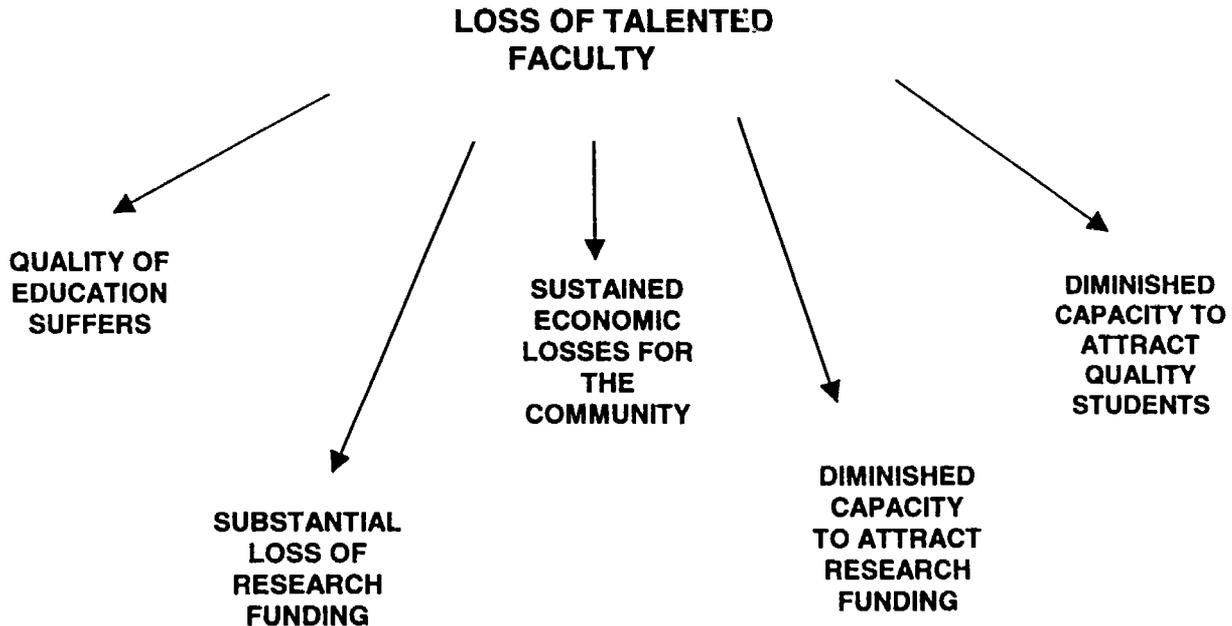
## FACULTY RETENTION

Faculty retention again was a significant problem for Arizona's universities in FY 02. Notwithstanding the economic situation throughout the country, an increasing number of faculty members left for positions in other organizations, often receiving much higher salaries and exceedingly better benefits.

As illustrated below, the universities and the communities they serve lose much when faculty leave Arizona. Top scientists and researchers may take millions of dollars in grants and contracts with them when they depart, setting university progress back by years and diminishing the university's ability to attract additional research funding. Moreover, when the universities' research efforts are curtailed, the economic consequences are substantial.

In Arizona, 39.5 jobs are created for every \$1 million in research contracts and grants to colleges, universities and professional schools, according to the U.S. Commerce Department's most recent economic analysis.

Equally important, educators who are leaders in their field contribute markedly to the quality of the educational experience for the many thousands of students in the Arizona University System. When the universities lose these leaders, the students lose out on the inestimable opportunity to learn from these scholars.



In regard to faculty turnover, the average turnover rates for all categories of faculty at ASU Main, ASU West, and ASU East are 10.2%, 14.4%, and 8.9% respectively. The faculty turnover rate at NAU is 12% and, at UA, the faculty turnover rate is 8.8% at the Main Campus and 9.2% at the Arizona Health Sciences Center.

It is difficult to compare Arizona's turnover rates to that of other universities since comparable, up-to-date, information for all categories of faculty for other universities is very difficult to obtain. However, two studies were identified that focused on turnover rates for tenured and tenure-track faculty, which reflected that the turnover rates for these two categories of faculty generally are low and stable, averaging about 5%.

In one of the studies, Harrigan (1999)<sup>2</sup> presents information gathered from the literature and from an e-mail survey. At 13 universities where the data was available, tenured and tenure-track faculty turnover rates ranged from 1.7% (University of Alaska) to 10.1% (University of South Dakota) with a mean of 4.9% and a median between 4 and 5%. More recently, the Texas Higher Education Coordinating Board conducted an extensive analysis of faculty turnover at Texas Public Universities.<sup>3</sup> For institutions with more than 500 faculty members, the rate was 5%.

While this year's turnover rate is a concern in and of itself, the cumulative effect of the turnover over the past several years is much more disturbing. Over the past three years, approximately 1,000 faculty members left the University System. The continuing loss of faculty saps the strength of the universities, weakening programs and research efforts and threatening the quality of the educational experience for Arizona's public university students.

It will take years to replenish and rebuild the reservoir of talented and distinguished faculty and intellectual capacity that the universities worked for so long and so hard to create.

To provide additional perspective, the three universities developed brief profiles of their faculty retention problems. In the next few pages, each university presents an array of statistical information and illustrative examples of the program implications associated with the loss of its faculty. The information pertains to tenured and tenure-track faculty and academic professionals who voluntarily considered leaving the universities last fiscal year. Retirements and other reasons for separation are not included in the analysis.

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<sup>2</sup> Margaret N. Harrigan (1999) *An analysis of faculty turnover at the University of Wisconsin-Madison*, presented at the 39<sup>th</sup> annual AIR Forum, May 30-June 2, 1999.

<sup>3</sup> *Faculty Turnover and Retention*, Texas Higher Education Coordinating Board, Division of Finance, 2001

# ASU FACULTY RETENTION FY 2002

## COLLEGES IMPACTED

Retention issues occurred at all three ASU campuses and in all colleges at ASU Main with the exception of Nursing.

## KEY POINTS

- During FY 2002, 120 faculty and academic professionals at ASU Main and 9 at the West and East campuses indicated that they were considering other jobs or had received job offers from other organizations.
- At ASU Main, this is a 60% increase over FY 2001 and a 167% increase over FY 2000 during which there were, respectively, 75 and 45 such faculty members.
- Of the 120 Main Campus faculty and academic professionals, 78 actually left for employment elsewhere.
- Fifty-five of the 120 individuals explicitly expressed that salary entered into their considerations, and the number of individuals who considered leaving escalated when the promised salary increases (5% + 5%) were rescinded during the budget debates.

Twenty-eight individuals shared details of offers made to them by other institutions. Competing institutions offered salary increases that were, on average, 30 percent higher than ASU salaries.

- ASU made counter or preemptive offers to 45 individuals. These counteroffers included, on average, a 16 percent average salary increase in addition to other perquisites. Thirty-two individuals who received counter or preemptive offers chose to remain at ASU.

## EXAMPLES OF PROGRAM IMPACTS

In the mathematics department, ASU lost three lecturers, one assistant, one associate and one full professor. One, a distinguished member of the mathematics faculty and the university administration, is leaving ASU for a position at Georgia Institute of Technology. He is a Regents Professor and has been a key player in helping to build the university's reputation, representing a large part of the reason that ASU is ranked 26<sup>th</sup> among public universities in applied mathematics by US News and World Report. Programmatically, applied mathematics is very important to ASU because of its emphasis on the engineering sciences. The individual was offered a \$40,000 increase in salary. Further, at Georgia Tech, the state's contribution to the optional retirement program is 30% higher than at ASU and the health plan offers a cafeteria of options as opposed to the single provider now used by the State of Arizona.

The loss of three key lecturers from the mathematics faculty has exacerbated a growing problem in offering enough sections of calculus and other lower division mathematics courses to a growing freshman class. All three lecturers went on to higher paying positions at community colleges or other universities.

- ASU was recently featured in the Chronicle of Higher Education for its exemplary leadership in fostering interdisciplinarity and for assembling faculty members from several disciplines to participate in its Long Term Ecological Research (LTER) Center.<sup>4</sup> This year ASU is losing two young scientists who are contributing members to the center, and a third has indicated that she will actively seek another position unless salary issues are addressed. These faculty members not only contribute to LTER but also are involved in instructional programs of a department that serves over 1,000 undergraduate majors and 80 graduate students.

A young assistant professor in the biomedical sciences has just been recruited away to the University of Missouri. He was offered a substantial increase in salary in addition to several other perquisites. This man was truly one of the rising stars and will take with him approximately \$500,000 per year in externally generated funding for research.

- Due to faculty losses, budget reductions, growing enrollments and the need to reallocate funds from empty faculty lines to address critical salary issues, the student to tenured and tenure-track faculty ratio has gone from 26 to 1 to 31 to 1 over the last 5 years. ASU is rapidly losing the ground it has gained in quality.

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<sup>4</sup> US Agencies Look to Interdisciplinary Science, Chronicle of Higher Education, issue dated June 14, 2002

# NAU FACULTY RETENTION FY 2002

## COLLEGES IMPACTED

Faculty retention and recruitment issues occurred in all colleges.

## KEY POINTS

During FY 2002, 24 faculty members indicated that they were considering other jobs or had received job offers from other organizations. NAU lost twenty-three of these twenty-four individuals.

- Salary was the most common reason for resignation. Faculty also noted related issues such as cost of living in Flagstaff and a spouse being unable to find adequately paid employment as additional reasons for leaving NAU.
- Counteroffers were made in only three cases since it was clear that counteroffers would not have prevented the resignations of the twenty-one other individuals. One counteroffer was accepted.
- For those cases where there was information on outside salary offers, competing institutions offered salary increases ranging from 18% to as high as 140%. One couple who left doubled their NAU salaries.

Community college salary offers are beginning to be competitive for faculty and academic professional staff, with Pima Community College hiring one of NAU's faculty members during the past year.

- A majority of faculty who resigned were Associate Professors and Assistant Professors, and 62% were tenured or tenure-track faculty.

Institutions that successfully hired faculty away from NAU included:

- Laurence Livermore National Laboratory
- Oregon Health Sciences University
- Southwest Texas State University
- Villanova University
- Washburn University
- University of Connecticut
- University of Victoria, Canada
- University of New Mexico
- University of Northern Colorado
- University of Arizona

**EXAMPLES OF PROGRAM IMPACTS**

- The Nursing Department currently is searching to fill six positions, as the department lost 4 faculty members last year and will hire two additional faculty members from Proposition 301 funding. The salary level NAU is able to offer complicates filling these positions. NAU's salary range of \$40,000-\$44,000 for doctoral-prepared Nursing faculty is not competitive in a market dominated by a national shortage. In Arizona, NAU not only competes with the other public universities but is also having trouble competing with the salaries of the Maricopa Community College system. Moreover, the College of Health Professions cannot eliminate even one position and use those salary savings to raise salaries to a more competitive level since the program would immediately be out of compliance with Arizona State Board of Nursing and national accreditation student/faculty ratio guidelines.
- In the Dental Hygiene program, NAU cannot accommodate the demand from dentists to increase the production of dental hygienists due to NAU's low salary base combined with the FY 2003 budget reductions.
- NAU lost one faculty member from its Exercise Science program and one from its Health Promotion program due to higher salaries elsewhere. This is a double blow since, not only did the programs lose excellent faculty members, but the College of Health Professions cannot replace them due to the need to respond to State budget reductions. Loss of the Exercise Science position likely will result in capping this

program, a step which is very unfortunate as it is one of the college's most popular majors. It currently has 253 freshmen and sophomore students declared as pre-exercise science majors and likely will have capacity to advance only 50 to junior status next year. Similarly, loss of the Health Promotion position will slow the development of what was a rapidly growing web-based Bachelor's of Applied Science degree program.

- NAU's undergraduate liberal studies program is organized around three foundation courses. One of those, the University Colloquium (UC 101), is designed to introduce students to the intellectual expectations of a university education and focuses on developing skills in critical reading, critical thinking, and effective writing. All colleges are asked to contribute faculty to teach the UC101 courses, with the intent that new entering students are exposed in a small, intense seminar to experienced scholars who represent a wide range of disciplines.

As NAU loses faculty through resignations and retirements and eliminates faculty lines, it is becoming very difficult to offer experienced faculty to teach UC101. Colleges face choosing between assigning faculty members to courses required by their majors and assigning them to UC101. In fall 1999, 76 percent of UC101 sections were taught by full-time, tenure and tenure-track faculty, and in fall 2001, the sections taught by this group declined to 22 percent.

- NAU's goal to increase the diversity of its faculty suffered a setback as five of the resigning faculty members (24%) were from an ethnic minority population.

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## UA FACULTY RETENTION FY 2002

### COLLEGES IMPACTED

- Every college except Nursing, Public Health and UA South negotiated the retention of faculty. (Public Health and UA South are relatively new programs.)
- The colleges of Agriculture, Business, Education, Engineering and Mines, Humanities, Law, Pharmacy, Science, Social and Behavioral Science, the University Libraries, Medicine and other non-college units all dealt with retention issues for 5% or more of their total faculty.

All main campus colleges were unable to retain faculty who chose to leave.

- On a positive note this past year, all of the colleges except Architecture were able to successfully retain some of their faculty who had better offers elsewhere.

### KEY POINTS

- During FY 2002, 125 faculty members indicated that they were considering other jobs or had received job offers from other organizations. This is a 39% increase over last fiscal year during which there were 90 such faculty members.
- This past year, retention issues involved 8% of the faculty campus-wide while in the previous two years it affected only 5%-6% of the faculty.
- For those cases where there was information on outside salary offers, faculty members were offered, on average, a 36% increase in salary in efforts to recruit them away.
- For those cases where there was information on UA counteroffers, the UA offered, on average, 15% more in salary attempting to retain faculty. Overall, UA expended almost \$700,000 in salary alone to retain faculty. This dollar outlay coupled with budget cuts adds an extra burden on colleges.

- For those cases where there was information on both the outside offers and UA counteroffers, the salary gap between the two offers was much higher for those UA lost (a 30% difference) than for those UA retained (a 13% difference).

In response to worsening competitive faculty salaries, the College of Engineering also gave college-wide preemptive retention dollars to 75 of their tenure-track faculty. These adjustments were in addition to the 125 other retention cases.

- UA lost faculty to public and private universities as well as to the private sector. Faculty were recruited away by the Universities of Michigan, Minnesota, Pennsylvania, and Wisconsin; and California institutions including the University of California-Berkeley, the University of California - Davis, and the University of Southern California. Other faculty also are now at Stanford, Harvard, and Notre Dame.

#### **EXAMPLES OF PROGRAM IMPACTS**

- The faculty recruited away in FY 02 generated \$10 million in sponsored research over the last 3 years. Those faculty that UA were able to retain in FY 02 generated \$75.9 million in sponsored research over the last three years. The university's continuing faculty retention efforts were critical this past year. While the university was able to retain top researchers this year, with one engineering professor producing \$23 million in research over the past 3 years alone, retention efforts must be continual because top institutions are continuing their efforts to recruit away the UA's top research faculty.
- A common theme this past year among faculty leaving was their concern about severe salary compression and the lack of resources for program development. With the budget cuts, faculty are concerned that key recruiting and appointments of new department heads will not take place. Faculty are distressed about the future of their departments. Even those faculty the university was able to retain this past year are still being courted by outside institutions.

It can be said that the University of Arizona is a training ground for better-financed institutions with the UA able to recruit outstanding faculty but unable to retain them. Based on a four-year average of survey data, those seeking outside offers are five years younger and have four years less experience than the UA faculty-at-large.

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- In the College of Science, of the three of the eight faculty who left, one was the largest grant earner with an internationally visible reputation, another was an excellent young scientist who was about to attain tenure, and the third was a distinguished scholar in the science of computational complexity, a sub-field of computer science dealing with complex mathematical algorithms that has direct applications for information security.
- The loss of a faculty member in the College of Social and Behavioral Sciences to the University of Michigan is jeopardizing the department's Title VI funding. The faculty member left because of frustration with the UA budget limitations related to recruiting and replacing key personnel.

## CLASSIFIED STAFF TURNOVER

Classified staff turnover is a chronic problem in the universities, with the universities losing far too many staff in positions that are critical to the operation and success of the institutions. These past twelve months alone, **over 1,800** classified staff members left their employment at Arizona's universities. Staff in such areas as information technology, libraries, public safety, health services, administrative support, and student services, to name a few, left the University System this past year.

Turnover is extremely disruptive and very costly. Each time a staff member leaves, the universities are faced with the advertising, interviewing, and training costs associated with hiring a new employee. In addition, many indirect, difficult-to-quantify costs exist, such as decreased productivity, loss of quality, and lost work hours when the job is vacant and while the new employee learns the new job.

A review of the literature reveals that the cost of turnover is generally estimated at one to two times the salary of a departing employee. With such high costs, the persistently high turnover rate in the universities is of much concern.

The chart below depicts the classified staff turnover rate in the University System.

### AVERAGE TURNOVER – CLASSIFIED STAFF

<u>UNIVERSITY/ABOR</u>	<u>TURNOVER PERCENTAGE</u>
ASU MAIN	16.1%
ASU EAST	3.4%
ASU WEST	15.3%
NAU	18.5%
UA MAIN	16.3%
UA HEALTH SCIENCES CENTER	21.4%
ABOR Central Office	28.6%*

\*Reflects that two out of seven classified employees separated from ABOR

## UNMET SALARY NEEDS

Using the methodology described earlier in this report, each university calculated its unmet salary needs at the end of FY 04. The calculations included the \$1,450 per FTE salary increase that took effect June 8, 2002 and the projected market movement.

As manifested by the chart below, university employees' salaries still will be considerably lower than those at peer institutions and in the other relevant markets by the end of FY 04. By June 30, 2004, an unmet general fund salary need of approximately \$157 million, including ERE, is projected in order for the universities to catch up with the market.

In 1996 when the university system developed its multi-year plan to restore salary competitiveness, universities estimated that it would cost approximately \$47.5 million dollars to reach the 50<sup>th</sup> percentile/market average. Today, six years later, the cost to raise the average salaries of current faculty and staff to the targeted level has escalated to \$157 million, and the situation will worsen dramatically if salary increases are not provided in FY 05 and FY 06. It is difficult to project market movement for these two future fiscal years. However, if the market continues to move as it has in the past from 4% to 5% a year, the unmet salary need will increase to approximately \$201.6 million by the end of FY 05 and to approximately \$247.7 million by the end of FY 06.

### PROJECTED UNMET SALARY NEEDS FOR THE UNIVERSITY SYSTEM AS OF THE END OF FY 2004

<u>UNIVERSITY SYSTEM</u>	<u>UNMET SALARY NEEDS</u>
ASU MAIN	\$52,169,400
ASU WEST	6,723,800
ASU EAST	2,285,700
NAU	31,027,700
UA MAIN	54,659,600
UA HEALTH SCIENCES CENTER	10,351,000
ABOR Central Office	181,500
<b>SYSTEM TOTAL</b>	<b>\$157,398,700</b>

## OVERTIME PAY

A.R.S 41-763.01 requires the Board of Regents to report on the universities' overtime pay. The overtime expenditures of each university and the Central Office of the Board of Regents during FY 02 are delineated in the chart that follows.

### OVERTIME EXPENDITURES

<u>UNIVERSITY/ABOR</u>	<u>COSTS</u>
ASU MAIN	\$270,700
ASU WEST	96,000
ASU EAST	15,900
NAU	66,187
UA MAIN	242,195
UA HEALTH SCIENCES CENTER	3,849
ABOR Central Office	0

## EXHIBIT 1

### PEER/COMPARATOR UNIVERSITIES

#### ASU/UA (combined)

University of California – Berkeley  
University of California – Los Angeles  
University of Michigan – Ann Arbor  
University of Maryland – College Park  
University of Virginia  
Rutgers, State University of New Jersey  
University of Connecticut  
University of North Carolina – Chapel Hill  
University of Illinois – Urbana  
University of Minnesota – Twin Cities  
Temple University  
University of Texas – Austin  
University of Illinois – Chicago  
University of Wisconsin – Madison  
University of Iowa  
Texas A&M University  
Ohio State University  
University of Washington  
Michigan State University  
University of Colorado – Boulder  
University of Missouri – Columbia  
University of Nebraska – Lincoln  
University of Florida  
University of Utah  
University of Kansas  
University of Cincinnati  
University of Oklahoma  
Florida State University

#### NAU

University of Delaware  
George Mason University  
University of Nevada – Las Vegas  
University of Nevada -- Reno  
University of Central Florida  
Old Dominion  
Oakland University  
California State University -- Fresno  
University of Minnesota -- Duluth  
Miami University of Ohio  
Ohio University, Main  
Bowling Green State University  
University of Vermont  
University of Wyoming  
Ball State University  
University of Montana  
University of North Dakota, Main

**ATTACHMENT C**

**Joint Legislative Study  
Committee on  
State Employee  
Compensation**

November 20, 2002

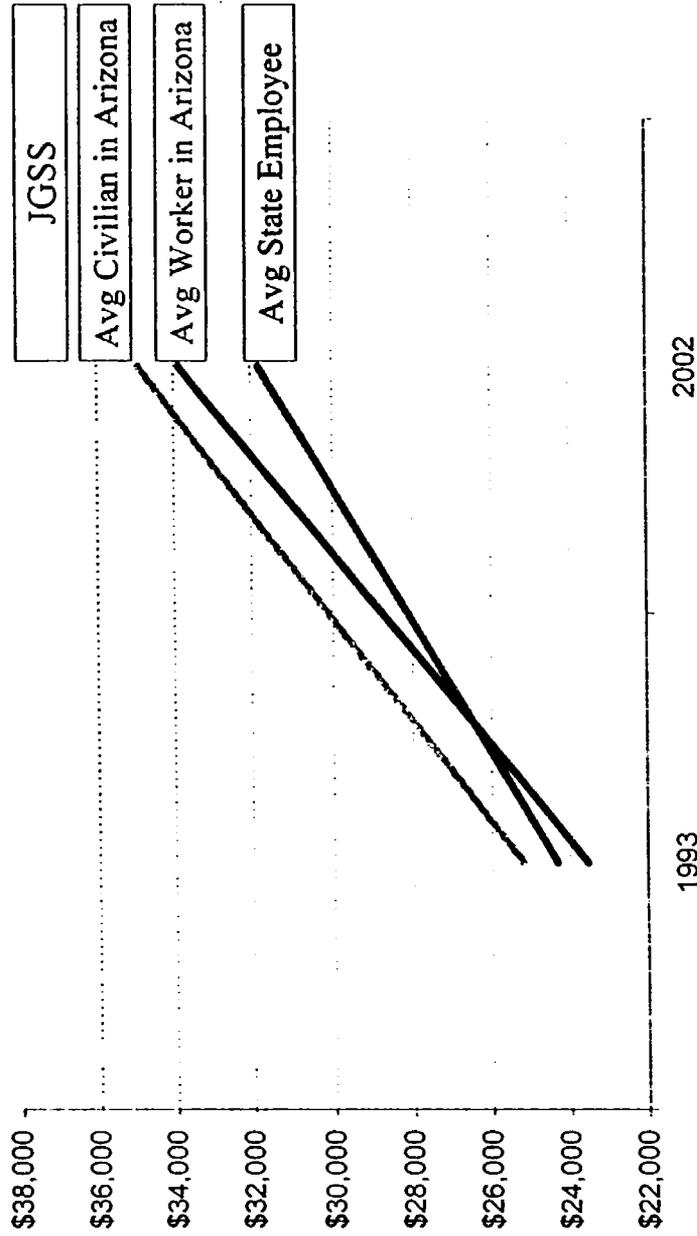
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## Market Comparison...

- JGSS shows the market exceeds employee salaries by 16.4%
  - ◆ Up from 13.2% just two years ago
- Western States shows the market exceeds employee salaries by 26.3%
  - ◆ Up from 15.8% two years ago

# We are behind in ALL Arizona benchmarks...

State Employee Salary Comparison



Source:

Joint Governmental Salary Survey, March 2002

Avg Civilian in Arizona, Civilian Wage, Eller College of Business, March 2002

Average Worker in Arizona, Bureau of Labor Statistics, Data from December 2000 projected forward using conservative 4%

Average State Employee, Human Resources Management System, June 2002

## **Key Indicators of Looming Problems...**

- Turnover of employees with less than 2 years of service was 62%
- Nearly 50% of employees have less than 4 years of service
- It takes an average of 10 years for an employee to reach midpoint

# Filled Positions by Agency....

	2001	2002	Difference
Small Agencies	967	967	2.1%
Administration	981	962	-1.8%
Agriculture	389	381	-0.4%
AHCCCS	1314	1388	5.5%
Attorney General	271	275	0.8%
Behavioral Department	51	52	2.0%
Building & Fire Safety	20	64	-0.1%
Conservation & Exploitation	43	41	-4.7%
Commerce	132	104	-20.5%
Corporation Commission	286	298	1.4%
Corrections	9449	9333	-5.7%
Economic Security	9844	10552	7.2%
Education	385	386	1.0%
Environmental Quality	791	750	-0.2%
Game & Fish	838	853	3.0%
Health Services	1825	1848	1.7%
Historical Society	91	84	-3.5%
Industrial Commission	300	291	-3.0%
Insurance Dept	138	140	5.1%
Juvenile Corrections	1238	1260	2.1%
Land Dept	230	235	0.8%
Liquor Commission	124	117	-3.6%
Medical Exam Board	75	75	3.1%
Military Affairs	494	507	2.8%
Parole	141	133	-3.7%
Posters Home	64	60	-6.3%
Recycling	65	65	0.0%
Real Estate	137	134	-2.7%
Register of Contractors	161	150	-5.6%
Retirement System	1051	1048	-3.4%
Revenue	1023	1048	4.1%
State Parks	248	251	1.1%
Transportation	4995	5000	0.1%
Veterans Service	285	288	3.1%
Water Resources	370	362	-2.0%
<b>Totals</b>	<b>39,488</b>	<b>39,506</b>	<b>0.0%</b>

- 11 agencies experienced reductions of more than 5%
- Excluding DES and AHCCCS, overall the State experienced a reduction of nearly 3%

**Comments:** The majority (over 60%) of state agencies (excluding the small agencies) remained the same or experienced a decrease in the number of filled positions. The Dept of Economic Security (DES) and AHCCCS experienced increases in the number of employees as a result of Proposition 204 that transferred hundreds of county workers to the state. Excluding DES and AHCCCS, the state experienced a nearly 3% reduction in workforce.

Source: The state's Human Resources Management System. 2001 and 2002 data represents fiscal year-end (July 1 - June 30). This table represents filled positions only - it does not include vacant positions.

# Rank Order of All States by Ratio of State Employment to State Population...

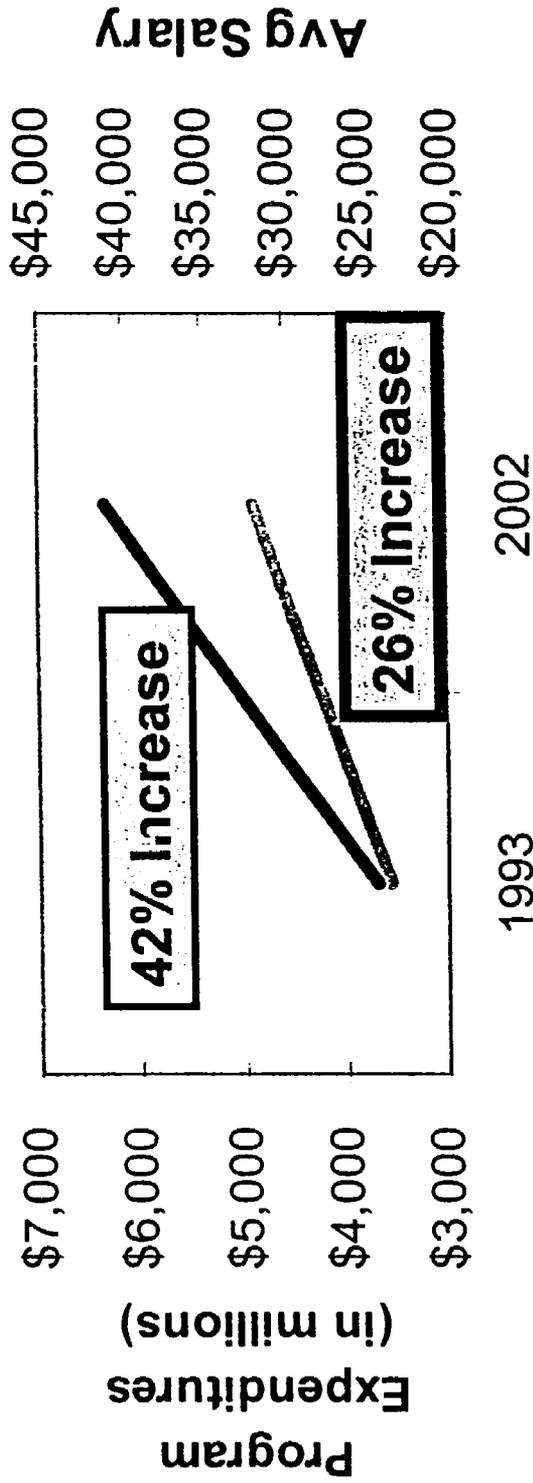
1	Hawaii	26	Virginia
2	Alaska	27	Missouri
3	Delaware	28	Maine
4	New Mexico	29	Kansas
5	North Dakota	30	New Jersey
6	Wyoming	31	Oregon
7	Vermont	32	North Carolina
8	Utah	33	Colorado
9	Louisiana	34	New Hampshire
10	Montana	35	Massachusetts
11	South Carolina	36	Minnesota
12	Mississippi	37	Georgia
13	Connecticut	38	United States Average
14	Washington	39	Michigan
15	Iowa	39	Tennessee
16	Oklahoma	40	Indiana
17	Rhode Island	41	New York
18	Kentucky	43	Arizona
19	Arkansas	44	West Virginia
20	Alabama	45	Ohio
21	South Dakota	46	Wisconsin
22	West Virginia	47	Florida
23	Idaho	48	Nevada
24	Nevada	49	California
25	Maryland	49	Illinois

43rd - ARIZONA

Comments: Arizona ranks 43rd in the nation in the ratio of state employees as compared to overall population of the state. Of the Western States, only California and Nevada have fewer employees as compared to overall population of the state.

Source: State Employment data from U.S. Census Bureau, Governments Division, March 2000. Population data from U.S. Census Bureau, Population Division, April 2000. Unpaid officials, pensioners, persons whose work is performed on a fee basis, and contractors and their employees are excluded from the count of employees.

# Investments in Employees haven't kept pace...



— Programs — Salaries

# Rank Order of All States by Ratio of Total State Payroll to State Population...

1	Alaska	26	Michigan
2	Hawaii	27	New York
3	Delaware	28	Idaho
4	Connecticut	29	Oregon
5	New Mexico	30	Alabama
6	Vermont	United States Average	
7	Rhode Island	31	West Virginia
8	North Dakota	32	Maine
9	Iowa	33	South Dakota
10	Washington	34	Kansas
11	New Jersey	35	North Carolina
12	Utah	36	New Hampshire
13	Louisiana	37	California
14	Wyoming	38	Wisconsin
15	Montana	39	Missouri
16	Colorado	40	Nebraska
17	Maryland	41	Georgia
18	Massachusetts	42	Pennsylvania
19	Kentucky	43	Indiana
20	South Carolina	44	Texas
21	Minnesota	45	Tennessee
22	Mississippi	46	Ohio
23	Virginia	47	Arizona
24	Oklahoma	48	Nevada
25	Alabama	49	Florida

47th - ARIZONA

**Comments:** Arizona ranks 47th in the ratio of total state payroll as compared to overall population of the state. Of the Western States, only Nevada has a lower ratio of total state payroll compared to the overall population of the state.

Source: State Payroll data from U.S. Census Bureau, Governments Division, March 2000. Population data from U.S. Census Bureau, Population Division, April 2000.

## **Our Recommendation...**

- Annual adjustments to base salary
  - ◆ Mid-point or market adjustments
  - ◆ Performance or merit increases
- Continue Salary Market Adjustments
- Lump sum cash payments for exceptional performers at maximum

**ATTACHMENT D**



**ADOA**  
Arizona Department of Administration  
**Self-Insurance Update**  
**November 20, 2002**

1. Proposed Legislation- Susan Strickler, ADOA
2. Status of RFP's- Susan Strickler, ADOA
3. RFP Timeline- Michelle Taylor-Brklacich, Mercer Consulting
4. Proposed Network Regions- Michelle Taylor-Brklacich  
Mercer Consulting

# DRAFT

## HEALTH INSURANCE TRUST FUND AND HEALTH INSURANCE ADMINISTRATIVE COSTS

**Contact:** Susan Strickler, Employee Benefits Manager  
Kathy Peckardt, Assistant Director – Human Resources Division

### **Proposal:**

A.R.S. § 38-654 would be amended to establish the HITF as an irrevocable trust, and to provide that funds deposited in the HITF are irrevocably dedicated to employee health insurance purposes.

In order to facilitate the administration of the self-insurance program, it is proposed to amend A.R.S. § 38-651 to provide that, while ADOA must establish policies governing the administration of the self-insurance program as well as the resolution of any disputes by an unbiased third party medical panel, such policies are exempt from the requirements of the Administrative Procedures Act (APA).

Strike A.R.S. § 38-654 D (4) which sets a rate on the administration costs per month.

### **Background:**

The Legislature has directed that ADOA self-insure employee health insurance by October 1, 2003. While ADOA currently has statutory authority to establish such a self-insurance program (A.R.S. § 38-651), statutory changes are needed to resolve or clarify several anticipated issues. First, A.R.S. § 38-654 establishes the Health Insurance Trust Fund to fund employee health insurance programs. Currently, appropriated funds deposited in the HITF may be removed and redirected by the Legislature for other purposes. As a self-insurance program cannot be established unless the State maintains sufficient reserves to meet several months anticipated claims, it is necessary to amend the statute to provide that these reserve funds may not be re-appropriated to other purposes. In addition, there is a question as to whether the policies and procedures relating to the self-insurance program's coverage, claims and other administrative matters are subject to the rule-making requirements of the APA, A.R.S. § 41-1001 *et seq.* The APA provides an extensive, formal process for the promulgation and amendment of agency rules requiring a minimum of six months. In addition, the APA provides that disputes regarding coverage must be resolved using the Office of Administrative Hearings rather than a review panel of medical professionals.

A.R.S. § 38-654 establishes the HITF and specifically, Section D. (4), stipulates that not more than \$1.50 per employee per month shall be used for

administrative purposes. There is and has been a conflict between this wording and the amounts collected via the contract for administrative and wellness purposes. The \$1.50 wording has been in statute prior to the administrative portion of the fund being appropriated, and thus served as a cap on administrative costs. However, since FY 1999, the administrative budget has been appropriated and the language has been ignored as appropriations were made that exceeded this cap. The current contract for medical insurance includes a \$4.10 surcharge, and the dental contract includes a \$1.00 surcharge, per employee per month, as a collection mechanism for administrative expenses. With the advent of appropriation status for the administrative portion of this fund, and particularly under self insurance, the amount (\$1.50) should be eliminated from statute.

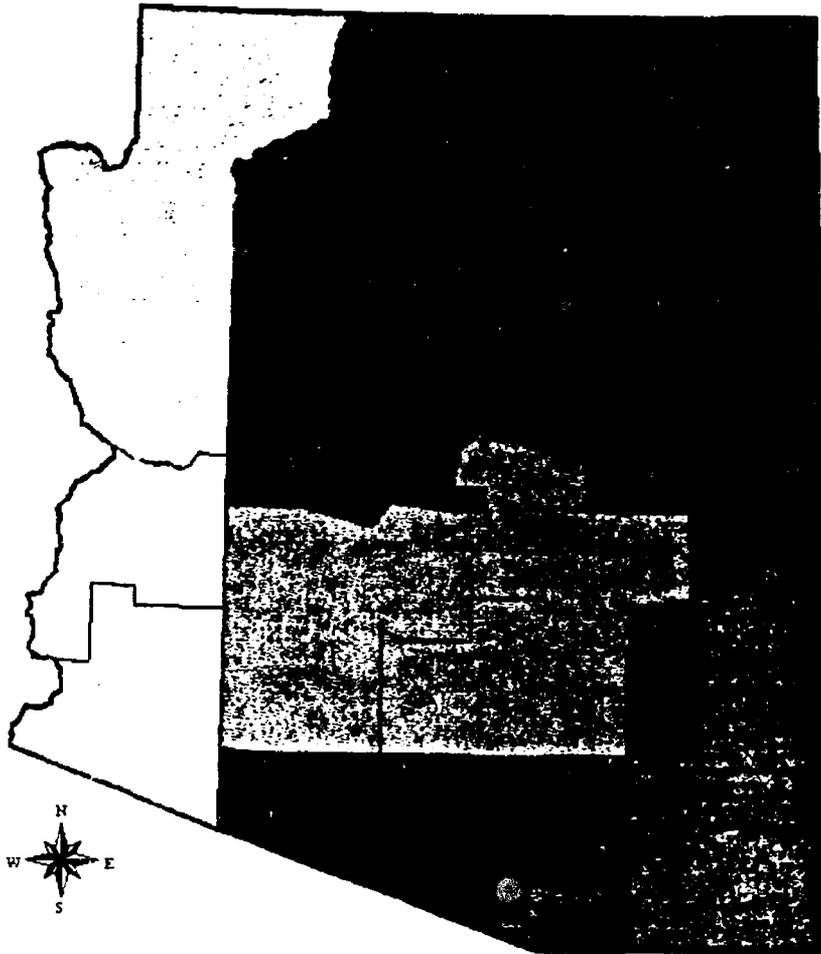
**Fiscal Impact:**

There is no fiscal impact since the appropriation supercedes this collection rate.

**State of Arizona  
Self-Insurance Vendor Selection Timeline**

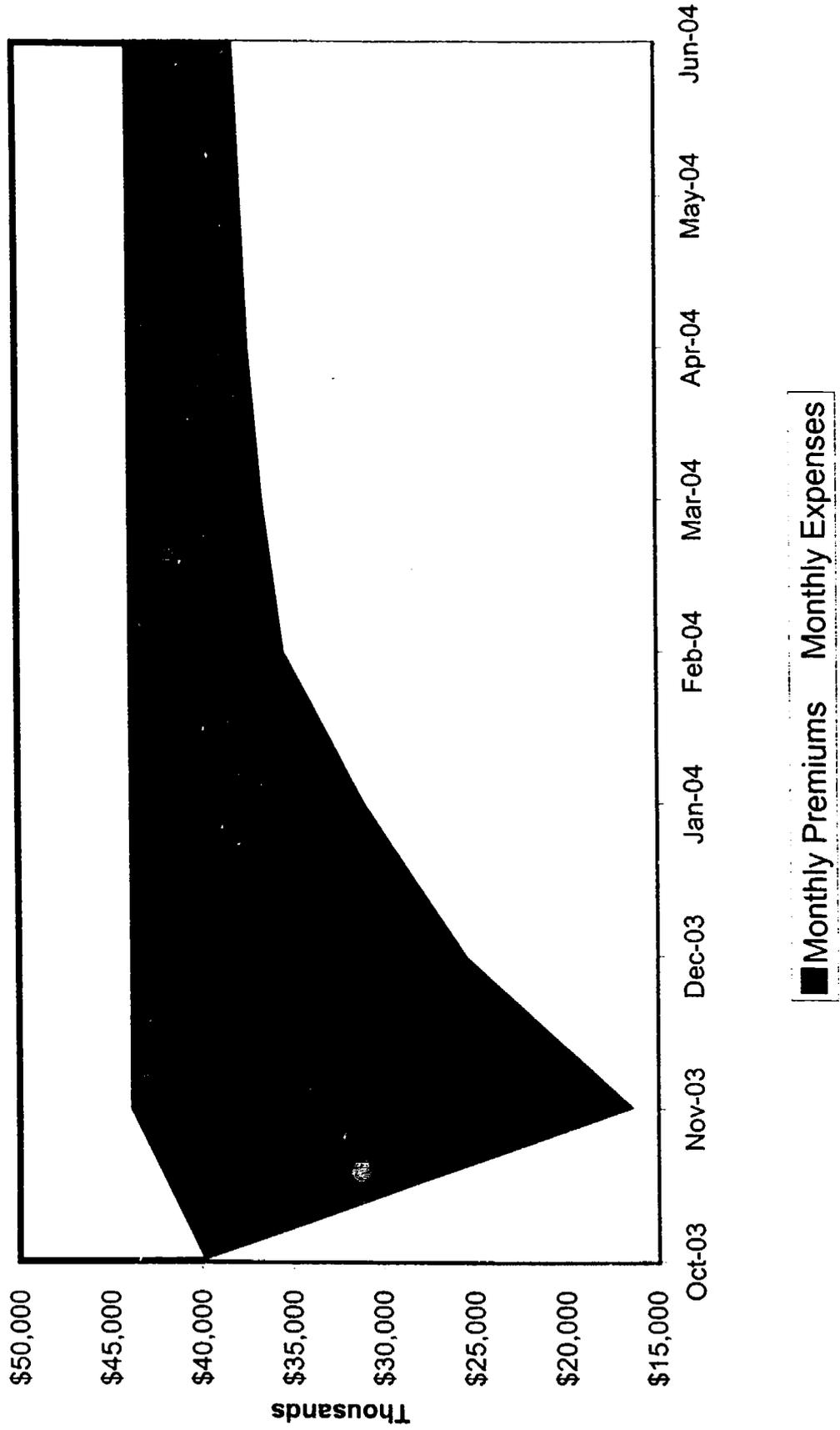
<b>Date</b>	<b>Activity</b>	<b>Responsibility</b>
December 2, 2002	State publishes Request for Proposal	State
December 16, 2002	Pre-proposal conference	State/Mercer/Potential Respondents
December 2, 2002 – January 8, 2003	Respondents complete RFP (hard copy and on diskette) and any related worksheets, and return signed documents to the State	Potential Respondents
January 9, 2003 – March 5, 2003	Evaluation Committee activities Respondent RFP evaluations Financial analysis	Representatives of State and Mercer
March 10-14, 2003	Finalist presentations	State/Mercer/Respondents
March 10-25, 2003	Negotiations	State/Mercer/Respondents
March 26, 2003	Send final contract documents to finalists for verification	State/Mercer
March 26-31, 2003	Finalists review contract documents and send final confirmation sign-offs to State	Respondents
April 15, 2003	Vendor award announcement	State
April 15, 2003	Vendor implementation begins	State/Mercer/Vendors
April 15 – August 17, 2003	Implementation coordination	State/Mercer/Vendors
August 18 – September 12, 2003	Annual enrollment period	State/Vendors
August 26, September 2, September 9, and September 16, 2003	State sends enrollment data to vendor(s)	State
September 26, 2003	Identification cards sent to State enrollees	Vendors
October 1, 2003	Plan year begins	State/Vendors

## Proposed Network Regions for Self-Insured Program



-  = NORTHERN REGION (Yavapai, Coconino, Navajo & Apache)
-  = WESTERN REGION (Yuma, La Paz & Mohave)
-  = CENTRAL REGION (Maricopa, Pinal & Gila)
-  = SOUTHERN REGION (Pima)
-  = SOUTHWESTERN REGION (Santa Cruz, Cochise, Graham & Greenlee)

# State of Arizona Self-Insurance Reserve Build-up



**ATTACHMENT E**

# ARIZONA STATE LEGISLATURE

## INTERIM MEETING NOTICE OPEN TO THE PUBLIC

### JOINT LEGISLATIVE STUDY COMMITTEE ON STATE EMPLOYEE COMPENSATION

**Date:** Friday, March 15, 2002  
**Time:** 2:00 p.m.  
**Place:** Senate Appropriations Hearing Room 109

#### AGENDA

1. Call to Order
2. Presentation on the Status of Self-Insurance – ADOA
3. Presentation on Uncovered vs. Covered Positions – ADOA
4. Update of State Compensation Ranking and Market Comparison – ADOA
5. Presentation on Pre-Paid Legal Services Benefits – ADOA
6. Other Business
7. Public Testimony
8. Adjourn

#### **Members:**

Senator Edward Cirillo, Cochair  
Senator David Petersen  
Senator Marsha Arzberger  
William Bell  
Sandra Williams  
Shawn Nau  
Linda Strock  
Carl Williams  
Alan Maguire

Representative Debra Brimhall, Cochair  
Representative Marian McClure  
Representative Victor Soltero  
Secretary of State Betsey Bayless  
Leigh Cheatham  
Cathy McGonigle  
Kathy Peckardt  
Pam Tenney

Persons with a disability may request a reasonable accommodation such as a sign language interpreter, by contacting the Senate Secretary's Office: (602)542-4231 (voice). Requests should be made as early as possible to allow time to arrange the accommodation.

ARIZONA STATE LEGISLATURE  
Forty-fifth Legislature – Second Regular Session

JOINT LEGISLATIVE STUDY COMMITTEE ON  
STATE EMPLOYEE COMPENSATION

Minutes of Meeting  
Friday, March 15, 2002  
Senate Appropriations Hearing Room 109 -- 2:00 p.m.

(Tape 1, Side A)

Cochairman Cirillo called the meeting to order at 2:05 p.m. and attendance was noted by the secretary.

Members Present

Senator Petersen	Representative Soltero
Senator Arzberger	Shawn Nau
Secretary of State Betsey Bayless (acting Governor)	Linda Strock
William Bell	Pam Tenney
Leigh Cheatham	Carl Williams
Alan Maguire	Representative Brimhall, Cochair
Senator Cirillo, Cochair	

Members Absent

Cathy McGonigle	Representative McClure
Kathy Peckardt	Sandra Williams

Speakers Present

Pam Culwell, Assistant Attorney General, Employment Law Section, Attorney General's Office  
Carolyn Friedman, Classification and Compensation Manager, Human Resources Division,  
Arizona Department of Administration  
Suzanne Stricker, Acting Benefits Manager, Arizona Department of Administration  
Steve Schramm, representing William M. Mercer Incorporated  
Ray Valenzuela, Executive Director, American Federation of State, County and Municipal  
Employees Council 97

Opening Remarks

Chairman Cirillo noted that a major portion of the meeting will be devoted to the study the Arizona Department of Administration (ADOA) is conducting on the possibility of self-insuring the state medical plan so the Members can provide input before the project goes any further.

## Presentation on Uncovered vs. Covered Positions

Chairman Cirillo noted that the topic of covered and uncovered status came up several times during prior meetings. An Attorney General's opinion relating to covering and uncovering of employees by the ADOA was mentioned so someone from the Attorney General's Office was invited to address the issue.

Pam Culwell, Assistant Attorney General, Employment Law Section, Attorney General's Office, noted that two questions were raised and addressed by the opinion:

- Are state employees covered by the merit system unless specifically exempted under A.R.S. Section 41-771?
- Does an agency have the authority to uncover a position that is not specifically exempt?

She related that the opinion states that all employees in state service are covered by the merit system. The definition of state service essentially equals the merit system and only excludes employees in exempt positions listed in statute. Exemptions can be constitutional or statutory. Certain exemptions in Section 41-771 were specified by the Legislature and include elected state officers, curator/curatorial aides, tour guides, people working in the State Capitol Museum, officers and enlisted personnel of the National Guard of Arizona, and patients or inmates employed in state institutions. There are 12 specific exemptions and a 13th for exemption of any other position exempted by law.

Ms. Culwell advised that the opinion addressed Section 41-771, subsection B, which provides for legislative granting of authority to the Director of the ADOA to determine if certain types of positions are exempt from the merit system according to eight categories of criteria that must be met. Those categories were discussed in the opinion, but the Attorney General's Office was not asked to consider if any particular uncovering was illegal or done outside the statute. The opinion basically deals with statutory construction and integration.

She stated that in summary, agencies do not have the authority to uncover, but the Legislature does, and within one section, the Legislature grants authority within certain guidelines to ADOA to make the determinations. For example, if there is not a specific exemption and the Director of the Arizona Department of Transportation (ADOT) wishes to uncover a top level position, the Director would have to make application to ADOA with an explanation of why the person falls within the exemptions allowed in statute.

Mr. Williams asked if an uncovering would be uniform within a department or apply to one individual among many in the same position. Ms. Culwell replied that it depends on why the position is uncovered. Some of the exceptions could be positions that are class wide. For example, if the department explains that someone provides legal counsel, the position is supposed to be exempt from the merit rules. If the position is part-time, that is pretty self-explanatory and there is not much discretion, but if the person is required to maintain a direct confidential working relationship, it could be one person out of a group of many or it could be a whole group of people.

Ms. Strock commented that she heard from someone who deals with human resource issues that the number of uncovered positions in the last few years increased from about 500 to around 6,000, which is significant; therefore, she would like to know the kinds of positions affected by the policy to uncover.

Chairman Cirillo noted that the opinion delineates the categories and gives some indication of the types of positions. He asked how the ADOR records reclassifications.

Mr. Bell indicated that he will find out and provide demographic data that is available. He related to Mr. Williams that when he was the Personnel Director at ADOA, agencies had to make requests to uncover positions in writing.

Mr. Soltero remarked that the Members should know what positions were uncovered and the basic reason. He speculated that the purpose was to increase salaries down the road.

Chairman Cirillo stated that when he worked in private industry, the terms "exempt" and "non-exempt" were used, and a determination was made depending on whether or not overtime must be paid to people, which is a legal problem, and management versus non-management people.

#### Update of State Compensation Ranking and Market Comparison

Carolyn Friedman, Classification and Compensation Manager, Human Resources Division, Arizona Department of Administration, related that ADOA recently began conducting two surveys that are performed annually. The Joint Governmental Salary and Benefits Survey is an Arizona survey and the Western States Salary Survey is a survey of positions normally only found in government. She apprised the Members that if state employees receive the two 5 percent increases originally appropriated at the end of FY 2003, salaries would still be over 14 percent off the market, and without the increases, salaries would be more than 27 percent off the market. She provided the following information:

- In March 2001, salaries were 16.4 percent off the market, and on April 1, 2001 a 2 percent merit increase was given, bringing salaries to 14.4 percent off the market.
- By the end of June 2001, there was a variance of 15.73 percent off the market.
- By the end of June 2003, aging the data, it is estimated that salaries will be off the market by 14.15 percent if the two 5 percent general salary adjustments are given. If the two 5 percent salary adjustments are not given, salaries would be 27.1 percent off the market.

Ms. Friedman stated that despite the downturn in the economy, organizations are worried about attracting and retaining employees so it is still important for many organizations to reward at least top performers because salary is one of the main reasons top performers leave.

Chairman Cirillo asked what is going on with the level of increases for Maricopa County.

Mr. Nau related that the budget is being prepared for next year. As in the past, efforts are being made to encourage departments to use data derived from the Managing for Results program to fashion gain-sharing programs to reward employees on the basis of departmental savings, which can be turned permanently back into the general fund. Incentive-type payments, one time in

nature, would be given during the next year in the event the department is successful in putting together such a program. He stated that the County is currently facing fairly dire circumstances in the budget, and since it is still not known how the state's budget will impact County budgets, a directive was sent to everyone, including the County's own health system, which is facing difficult circumstances, not to load any amounts in the budget for base increases. He opined that because the state continues to face difficult circumstances, serious consideration should be given to the possibility of one-time payments in the form of incentives from cost savings and review of the flexibility given to departments to provide increases to maintain higher performers. If the current system continues in which almost everyone receives about the same amount unless the position is uncovered, the really good people will leave and the low performers will remain because a raise is received without being a high performer.

Ms. Friedman added that in FY 2000 the state employee turnover rate was 17.09 percent. Last fiscal year it was 17.38 percent and it is down for the first half of 2002 to 15.3 percent. She noted that when the economy is bad, turnover rates decrease, but the question that needs to be asked is if the right people are staying versus leaving. She advised Chairman Cirillo that the results of the two surveys should be available in July 2002.

Ms. Strock commented that while reviewing some of the pay data, she was struck by the fact that state pay lags the market more today than when the Committee started so she believes a long-term solution would be legislation requiring that the budget, when introduced, should include money for market movement predicated on the idea that pay should not remain static and a system is needed to allow the money to be in the budget. She said she would like the issue to be included on the agenda for the next meeting.

Chairman Cirillo remarked that while it is wonderful to do all the comparisons to the outside, the comparisons are made in order to adjust the ranges, which is not done in most cases. There should be a procedure whereby state salary ranges raise simultaneously with those given on the outside, which would also help with the compression problem.

Mr. Soltero stated that he does not believe anyone would have a problem with Mr. Nau's suggestion that the state consider incentives or pay for performance; however, before proceeding in that direction, salaries should be raised to a decent, respectable level and people who deserve a bit more could be moved up.

Mr. Nau said he does not disagree, but pointed out that the County did not fully fund huge market increases initially, but changed the system to allow departments to experiment with small amounts of money in giving increases based on needs. He noted that some departments require many relatively inexperienced, low-skilled people at relatively low wages while others need a handful of high performers who must be retained in order to survive. The state probably has the same problem, yet the compensation system is basically "one size fits all." He was not arguing for pay for performance alone, but flexibility for departments to make choices as to the kind of compensation strategy that is needed in order to fit department needs, and doing that without money first is better than giving a lot of money right away. He added that if there is not much money this year and next, this would be a good time to begin that kind of strategic approach.

Mr. Nau advised Ms. Brimhall that the County's plan was adopted in July 1997 with the goal of being within five percent of mid point on average within five years. For the first two years, the normal practice of funding very small amounts of raises continued. Department directors were able to get a sense of how the system works and could use some salary savings associated with turning in or deleting positions to give increases. In the fourth and fifth years, increases were scaled back again, and this upcoming year, it looks like there will not be any. He said while the final data is not totally available, it looks like the plan has been successful. Salaries are probably not within 5 percent, but around 7 or 8 percent, which is still behind market, but an improvement over 17 to 18 percent behind market in 1997. He related that in 1996, the turnover rate was 29 percent, but by the time the five-year strategy was over, it was under 10 percent. He has not seen current data, but was told that it is now 6 percent or lower.

Ms. Brimhall said she was told by one person who works for the state that she is doing the job three people were doing, but after more discussion, the person admitted that she is doing the job it used to take three people to accomplish, but should not have. She added that one of the reasons the state has higher turnover rates is that interns and pages, who are not permanent state employees, are included in the calculation, as well as other seasonal or temporary people. She asked if that if the County includes those types of employees.

Mr. Nau responded that the B&A statistical method is used to calculate turnover rates. It was intentionally chosen because the model does not include temporary employees.

Mr. Bell countered that the Personnel Division at the ADOA does not count seasonal or temporary employees in turnover figures; therefore, pages and interns in the House, for example, would not be included.

#### **Presentation on Pre-Paid Legal Services Benefits**

Chairman Cirillo related that the Members discussed other benefits that might be offered to employees and one suggestion was pre-paid legal services. He asked for an update on the matter.

Mr. Bell advised that the ADOA received material from companies that want to do business with the state in this particular area. He pointed out that such a program would have to be bid, which would require some time. Also, payroll deduction capability would be necessary, but the payroll personnel system is currently undergoing a revamping and new capacity cannot be added to the old system. As a result, implementation of pre-paid legal services is currently on the sidelines.

Chairman Cirillo asked that Mr. Bell provide more information on pre-paid legal services, as well as any other potential programs that would not impose a cost to the state, but would provide a service to employees, when the Committee meets again in September 2002.

#### **Presentation on the Status of Self-Insurance**

Mr. Bell related that the ADOA is studying the issue of self-insurance and has been meeting with representatives from William M. Mercer Incorporated who are present today to convey the opportunities and challenges associated with moving in that direction.

Suzanne Strickler, Acting Benefits Manager, Arizona Department of Administration, added that the ADOA talked to several consulting groups about everything from structure to what the state would have to do financially should a decision be made to go to self-insurance. She introduced Steve Schramm.

Steve Schramm, representing William M. Mercer Incorporated, introduced other members of the Mercer team present in the audience and reviewed a handout regarding the Status of Self-Insurance (Attachment 1).

(Tape 1, Side B)

Senator Petersen noted that when the state changed to CIGNA as the sole health insurance carrier, some different options were promised by the next enrollment period. He asked if CIGNA will be used again next year.

Mr. Bell replied that CIGNA recently submitted costs for next year. ADOA plans to meet with CIGNA executives next week to see if an agreement can be reached that will benefit the state and employees; otherwise, going to bid is a possibility.

Senator Petersen asked how many other states across the country of similar size already self-insure.

Chairman Cirillo noted that the issue was discussed in several other committees and every state larger than Arizona, except New York, is self-insuring.

Mr. Schramm related that Mercer conducted a survey of other states, which can be provided to the Members, but 34 of the 50 states currently self-fund at least one benefit plan.

(Tape 2, Side A)

In response to a query by Ms. Brimhall, Mr. Schramm advised that the state will have to determine which functions (plan design, benefit decisions, vendor selection, appeals processes, medical management, formulary determination, etc.) should be done in-house or contracted, noting that some are very complex and pose the risk of liability. He added that a key finding of the survey of other states is that almost every state contracts at least some portion of management of the self-insured program.

Chairman Cirillo submitted that actual payment to the employee is something that should probably be contracted.

Mr. Schramm related that according to the survey, only the State of Louisiana actually pays its own claims. Every other self-insured state contracts the claim payment process. He advised Ms. Brimhall that the typical third-party administrative function associated with claims payment covers submission, adjudication, and pending associated issues. Disputes about medical necessity associated with the service are typically covered separately under a medical management contract, utilization review, or utilization management contract. He offered to present more detailed information on the matter in a later forum.

Ms. Brimhall acknowledged that she would like more detail since she understands the private sector realizes a greater savings by not allowing settlement to be done by an outside contractor. An outside source who pays claims could set a predetermined value and gain additional income if claims can be settled for less.

Mr. Schramm responded that a potential advantage of going to self-insurance is the ability to control the fee schedule, contracting process, adjudication rules, reimbursement schedule, etc. Typically, when contracting with a fully insured partner, there is reluctance to customize a certain percentage of infrastructure because that is their approach, but it is not without cost to do complete customization. He noted that if the state wants the claims adjudication process to be the exact amount the provider would be reimbursed, the issue would be discussed with the ADOA for program design.

He related to Senator Petersen that he does not know if task forces to develop program recommendations in other states took four to six months to accomplish the task, but having had the opportunity to participate in multiple task forces in the last 18 months for the State of Arizona, he believes the time frame is fairly reasonable (Attachment 1, Page 5). He clarified that the timeline would begin from the official decision date. Discussion followed.

Ms. Strickler related that the ADOA looked at a timeline in which various items need to be accomplished. She advised that the statute already allows the state to self-insure so legislation would only be needed to shore up the health insurance trust fund or codify items that would be necessary to make the program the most successful.

She noted that the biggest part of the timeline developed is communication with state employees. The average employee fears that self-insurance will be another "alternative fuels" or that it will solve all of the problems, i.e., those experienced with CIGNA. She opined that self-insurance needs to be communicated at every level so employees have a comfort level with what is going on. Various other parts of the timeline include printing material, establishing the open enrollment process, infrastructure, staffing, budget proposals, etc. Most other states implemented self-insurance in the 1980s so it is difficult to find out what was done at that time because people involved no longer work there. Some states have had very successful results and some have extremely politically bad problems. She added that the timeline includes visits to other states to see what does and does not work so the best practices can be used.

Ms. Strickler related to Ms. Brimhall that the task force is actually a working group to review the different processes. The working group may decide legislation is necessary to resolve some issues, but the group could begin working this summer so items will be in place once self-insurance is implemented. She pointed out that if a decision is made to go forward with self-insurance, it will not be implemented in October 2002, but during the following open enrollment in 2003. The possibility of self-insurance was considered for October 2002, but Mercer and two other consulting firms that specialize in this area said it would be foolish for the state to push the program through, especially considering the current market in the medical community and the situation of the state. It is important to go forward slowly and implement everything properly.

Mr. Maguire revealed that he and a few other people in the audience were around when the Arizona Health Care Cost Containment System (AHCCCS) was formed, and he considers a conversion to self-insurance, particularly as discussed in this presentation, to be as complex, if not more complex, than that endeavor. That process took well over three years to be effectively completed and caused the bankruptcy of a very large, independent company in the process; therefore, it is absolutely unbelievable that someone would consider discussing a transformation of health insurance, which is one of the most important items to state employees, between now and the fall. He contemplated three to five years for implementation.

He submitted that since there is no reason to believe money will be saved by self-insuring, good data is needed; otherwise, this entire conversation is premature. The problem with health insurance bidding at the state level is that the character and behavior of people who use insurance is not understood. Uncertainty for insurance companies has been radically increased because of the way the markets have been artificially constrained and legislative intervention in forcing bids that are not market driven, which caused prices to increase. This conversation is trying to cure a problem that does not exist instead of curing the problem that does exist, which is lousy data about utilization. AHCCCS was a failure in the beginning and a success later on after obtaining good data on applicants.

Mr. Maguire noted that the AHCCCS legislation took over two years to draft and was redrafted at least twice after the agency was in place. He opined that it is a fundamental error to discuss the issue of self-insurance to take over the insurance aspect of health care costs simultaneously with benefits because those are two entirely distinct issues that are glued together in the private insurance market, but the advantage of self-insurance is that they can be severed. He submitted that in relation to the key advantages and disadvantages, he does not believe the presentation fairly represents potential risks. He believes self-insurance is a good idea, but it is also incredibly complicated and will take a very, very long time. He cannot imagine that a health care program can be administered for state employees at a lower cost than the private sector because the pure negative economies of scale will force the cost up. He added that the lack of availability of health care in rural Arizona, which drives costs up, has not been discussed.

Mr. Bell agreed. He stated that the purpose of the presentation is to give the Committee some indication that the ADOA takes the charge of looking at the possibility of self-insuring seriously. This is an incredibly difficult issue, which is why Mercer was consulted. The presentation is part of the process to eventually make the decision of whether or not self-insuring is a good idea, but considerably more data is needed before a decision is made.

Ms. Brimhall voiced the fact that constituents are frustrated and angry and want to know what the state is going to do by October 2002 when open enrollment occurs.

Chairman Cirillo asked if more demographic data is available than last year to help the ADOA in negotiations with CIGNA.

Mr. Bell responded that some figures were recently received from CIGNA, but there has not been an opportunity to go through the material and begin the negotiation process. He hopes to do that next week, and sometime after that, he will be able to be more specific about the ADOA's

expectations and whether or not the state will be doing business with CIGNA or consider going to bid.

Chairman Cirillo opined that chances of obtaining demographic data would be better if the state controlled the plan because health insurers currently have all of the data.

Mr. Maguire agreed, noting that part of the process is taking a step back and looking at what works and does not work under the current system. It has been a long time since he was involved with AHCCCS, but very, very detailed requirements for utilization reporting were put in place years ago and the information continues to improve. Items like that would help in terms of bidding exercises, but part of the reason it can be difficult is that there are many requirements in terms of how to structure the bid that are not placed on AHCCCS providers; therefore, it is easier to be an AHCCCS bidder than a state health bidder. People walked away from the bid last year stating that the state asked for items that are completely unrealistic. There is a tremendous impact because substantial communities in the state have only a single provider, which gives that provider infinite monopoly of power in the bidding process. The insurance company contractor is put in an impossible position and exposed to huge amounts of risk that are not necessary, none of which will be addressed by self-insurance. He said it is difficult to believe that if self-insurance is implemented, the state will be more effective at negotiating under those circumstances in those communities; in fact, once the situation becomes known, the assumption would be to raise prices virtually infinitely.

Mr. Williams asked how information would be communicated to current state employees and retirees.

Chairman Cirillo said possibly letters could be sent to employees and bulletin board announcements posted. Retirees would only be contacted if a decision is made to include them in the package, which he would like to do, but that would require a lot of effort.

### Public Testimony

Ray Valenzuela, Executive Director, American Federation of State, County and Municipal Employees Council 97, thanked the elected officials on the Committee for supporting state pay raises, noting that the battle continues. He made the following points:

- Uncovering is a problem that will have to be reviewed more in-depth because, from information he received, some employees were exempted while others doing identical work were not and were actually solicited to sign forms to go uncovered with the carrot of some salary adjustments.
- Regarding health insurance, more information is needed from employees actually affected by these decisions; however, much of the criticism received in general is that employees want more options of carriers, through a statewide contract or not, rather than more options under the same carrier.
- One Arizona Department of Economic Security (DES) employee has to choose between paying the mortgage or health insurance payment, but she was told that her insurance cannot be stopped until the next enrollment period.

Chairman Cirillo suggested that the employee contact Mr. Bell's office.

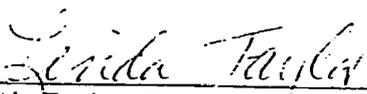
- Regarding self-insurance. not too long ago a candidate talked about a "locked box" so he hopes the Members will lock that box, too, as in the Arizona State Retirement System.
- An opinion that appeared in The Arizona Republic from Jack Pfister is right on point (Attachment 2).

Mr. Valenzuela noted that when the Committee first began, a determination was made that benefits were competitive to some extent with other jurisdictions, but salaries were the main problem. It is alarming to hear that the situation may be worse now than when the Committee was created. He said he does not believe state employee salaries will be brought within 5 percent of market value by 2003 as intended, but efforts should continue in that direction. He added that he is willing to work with the state to make sure the issue is ultimately addressed.

### Closing Remarks

Chairman Cirillo opined that it is important to get issues on the table. The Committee will continue to work with the ADOA, but on dual paths, because Mr. Maguire's comments are very appropriate that self-insuring, which is a good thing to do, will not solve a lot of the other problems. but may provide the option of an easier way to obtain some of the data needed before making a decision to go to self-insuring.

Without objection, the meeting adjourned at 4:00 p.m.

  
\_\_\_\_\_  
Linda Taylor, Committee Secretary  
March 21, 2002

(Original minutes, attachments, and tapes are on file in the Office of the Chief Clerk.)

**ATTACHMENT F**

Agendas can be obtained via the Internet at <http://www.azleg.state.az.us/iagenda/iagenda.htm>

## ARIZONA STATE LEGISLATURE

### INTERIM MEETING NOTICE OPEN TO THE PUBLIC

#### JOINT LEGISLATIVE STUDY COMMITTEE ON STATE EMPLOYEE COMPENSATION

**Date:** Wednesday, November 20, 2002  
**Time:** 10:00 a.m.  
**Place:** Senate Appropriations Room #109

#### AGENDA

1. Call to Order
2. Presentation of State Compensation Ranking and Market Comparison – ADOA
3. Update on Status of Self-Insurance – ADOA
4. Other Business
5. Public Testimony
6. Adjourn

#### **Members:**

Senator Edward Cirillo, Cochair  
Senator David Petersen  
Senator Marsha Arzberger  
William Bell  
Sandra Williams  
Shawn Nau  
Linda Strock  
Carl Williams  
Alan Maguire

Representative Debra Brimhall, Cochair  
Representative Marian McClure  
Representative Victor Soltero  
Secretary of State Betsey Bayless  
Leigh Cheatham  
Cathy McGonigle  
Kathy Peckardt  
Pam Tenney  
William J. Adams, Jr.

Persons with a disability may request a reasonable accommodation such as a sign language interpreter, by contacting the Senate Secretary's Office: (602)542-4231 (voice). Requests should be made as early as possible to allow time to arrange the accommodation.

# ARIZONA STATE LEGISLATURE

## JOINT LEGISLATIVE STUDY COMMITTEE ON STATE EMPLOYEE COMPENSATION

**Minutes of the Meeting**  
**Wednesday, November 20, 2002**  
**10:00 a.m. , Senate Appropriations Room #109**

### **Members Present:**

Senator Edward Cirillo, Cochair  
Leigh Cheatham  
Alan Maguire  
Cathy McGonigle  
Shawn Nau  
Kathy Peckardt  
Linda Strock  
Pam Tenney  
Carl Williams  
Sandra Williams

Representative Debra Brimhall, Cochair  
Representative Marian McClure

### **Members Absent:**

Senator Marsha Arzberger  
Senator David Petersen  
Secretary of State Betsey Bayless  
William Bell

Representative Victor Soltero

### **Staff:**

Nadine Sapien, Senate Research Analyst  
Dallas Gold, Assistant Research Analyst

Senator Cirillo called the meeting to order at 10:05 a.m. and attendance was noted.

Senator Cirillo stated that there would be an Annual Report presented by the end of the year. The report will contain the recommendations of the Committee for salaries for next year. Senator Cirillo further commented that the Committee is effective in statute until the end of 2003 and hopefully it will continue further. He expressed his appreciation to everyone for all of their hard work.

### **Presentation of State Compensation Ranking and Market Comparison — Arizona Department of Administration (ADOA)**

**Joanne Carew, Classification and Compensation Manager, ADOA Human Resources**, presented a handout entitled "Joint Legislative Study Committee on State Employee Compensation" (Attachment A). Her testimony came directly from the

handout. Ms. Carew stated that the salaries for State employees continue to fall farther behind the market.

In response to Senator Cirillo, Ms. Carew stated that the State is now 11.4% behind the market.

In response to **Shawn Nau**, Ms. Carew stated that the 62% employee turnover for employees with less than two years of service is all voluntary.

In response to Senator Cirillo, Ms. Carew stated that she would make available the figures for voluntary and involuntary turnover rates.

Ms. Carew commented that the need for State services becomes greater in bad economic times and the agencies are experiencing reductions in employees of up to 3% and 11 agencies experienced reductions of more than 5%. She stated that turnover is now down due to the sluggish economy but steps need to be taken to be prepared for when the economy does turn around. The general public loses out because the State is not able to provide the people to provide services. She further noted that the State now has the opportunity to narrow the gap as competitors are not paying large salary increases due to the economy.

Ms. Carew presented another handout entitled "ADOA Human Resources System 2002" (Attachment B) and stated that their goal is to have salaries within 5% of market.

Senator Cirillo stated that there are still some areas of employment such as legal and engineering that are paying higher salaries to recruit State employees.

**Ms. Kathy Peckardt** commented that in 2002 there was a 12.7% turnover rate overall and 9.1% of this figure was a result of resignations, .8% were for retirements, and 2% were terminations. Ms. Peckardt further commented that Arizona has one of the highest rates of turnover in the nation.

**Ms. Cathy McGonigle, Human Resources Administrator, Arizona Board of Regents**, presented a handout entitled "Annual Personnel Report for the Arizona University System" (Attachment C). Her testimony came directly from the handout. She commented that this report relates to turnover, faculty recruitment, retention problems and the faculty and staff salaries compared to the market.

In response to Senator Cirillo, Ms. McGonigle stated that they are able to reallocate funds to adjust salaries to retain faculty members.

In response to Senator Cirillo, Ms. McGonigle stated that she would get the figures for voluntary turnover.

Ms. McGonigle stated that the dollar value of the benefit package for faculty is substantially lower than other universities.

Representative Brimhall commented that the unfair treatment of State retirees contributes to the turnover rate. She further commented that the retirement benefits must be a part of the employment package.

Senator Cirillo commented that the State's retirement package is pretty good compared to other companies.

Mr. Williams commented that he receives a lot of complaints about the quality of health care from the rural areas.

Senator Cirillo reiterated that the recommended dollar amounts to meet employment goals will be included in the final report.

In response to Representative Brimhall, Senator Cirillo commented that it is in statute to reach a goal of coming within 5% of the market.

#### **Update on Status of Self-Insurance — ADOA**

Senator Cirillo commented that every state the same size as Arizona, except New York, are now self-insured. He further commented that it is mandated in the last budget to ADOA to convert to self-insurance by October of 2003.

**Susan Strickler, Benefits Manager, ADOA**, presented a handout entitled "ADOA Self-Insurance Update" (Attachment D). Her testimony came directly from the handout. Ms. Strickler remarked that ADOA is advocating a one-year delay on the implementation of self-insurance due to the concern for the reserve fund. Ms. Strickler stressed that they want to protect the monies in the Health Insurance Trust Fund from being redirected by the Legislature for other purposes.

Senator Cirillo implied that the options are stopping all self-insurance efforts, a three-month delay for self-insurance, or continue with the one-year delay. He further commented that the one-year delay is probably the only viable option.

In response to Representative Brimhall, Ms. Strickler stated that ADOA is working to implement self-insurance by October of 2003 in case the delay is not granted and they are negotiating with CIGNA on a one-year renewal. She further said that the figures would be available soon as to what the renewal costs will be.

Senator Cirillo stated that in the proposed current budget there is an increase in cost of the health insurance premiums for this year.

Representative Brimhall indicated that she would like the projections and comparisons as to what the savings will be if the State is self-insured by 2003 and what the additional costs will be if delayed.

In response to Ms. McGonigle, Ms. Strickler noted that the early projections indicate that the savings in the first year of self-insurance would be approximately \$10 to \$13 million dollars.

Senator Cirillo stated that the savings will come by changing the offerings of the health insurance such as more options for higher deductibles and more co-pays. Ms. Strickler responded that this will be addressed along with the financial impact of these changes. They are discussing that with the delay of the appropriation of \$1.5 million for the implementation, it will be non-lapsing so all of the issues can continue to be reviewed.

In response to Mr. Williams, Ms. Strickler commented that the employee costs will be added into the total premium and the proposed contribution strategy will be reviewed by the Legislature.

Ms. Strickler explained that in the rural areas outside of Maricopa and Pima counties, they receive the PPO plan for the same costs as the HMO plan in Maricopa and Pima counties, which is \$25 a month for single and \$125 a month for family coverage. She further commented that due to low salary increases, they have tried to keep the costs of health insurance as low as possible.

Ms. Strickler introduced **Michelle Taylor-Brjklacich, Mercer Consulting**, and explained that she is the consultant working with ADOA on this project and will discuss the timeline for the self-insurance. Her testimony came from Attachment D.

Ms. Taylor-Brjklacich explained that the State would be divided into five network regions with the hope of having two networks available in every region. They based this proposal on the success of the Arizona Health Care Cost Containment System (AHCCCS) in developing their networks by dividing the State.

Senator Cirillo commented that it would give providers for the whole State, which in some areas are not good. The State would be contracting with several organizations.

In response to Representative Brimhall, Ms. Taylor-Brjklacich stated that this network region proposal does not preclude one network from being contracted with in every single region. She further commented that the rural providers are reimbursed differently than in Maricopa and Pima County. In the outlying areas, the providers are paid a fee for service at a much higher rate than in Maricopa and Pima counties where there is more competition. Therefore, the outlying physicians are reimbursed at a different percentage.

In response to Representative Brimhall, Ms. Taylor-Brjklacich pointed out that in the proposals for the network coverage, bidders in urban areas will receive better consideration if they also provide coverage in the outlying counties.

Representative Brimhall noted that this has not worked in the past and emphasized that the State should have more of a variety of plans to help ensure there will be providers for the outlying areas.

Ms. Taylor-Brijklacich commented that Mercer has met with carriers to discuss setting up different options in different areas and the response has been positive for bidding statewide.

In response to Ms. McGonigle, Ms. Taylor-Brijklacich stated that the plan is to have the data as one risk pool. There would be more control and access to the data by going to self-insurance.

**Mr. Alan Maguire** commented that he has grave concerns about self-insurance. Mr. Maguire explained that the concept of plan redesign is completely separate from the concept of self-insurance. Self-insurance is about risks and reserves. Mr. Maguire maintains that the concept of providers and networks is plan redesign and does not require self-insurance to be completed. Mr. Maguire further commented that AHCCCS is a fundamentally different type of model than a health care system that has voluntary participation and is different than a private health insurance provider. Mr. Maguire indicated that it is too expensive to practice in rural Arizona due to the lack of facilities and the corresponding medical malpractice risks that comes from this. He further explained that the State has no capacity to put the reserves aside that are necessary to make a self-insurance product viable. Mr. Maguire stated that the concept of risk pools must be addressed for all retirees and all employees at the same time.

In response to Representative Brimhall, Mr. Maguire stated that the State has not been able to deal effectively with insurance companies because the State has not tried. The State has put artificial constraints on the bid process at ADOA. Mr. Maguire reiterated that the bid process needs to be fixed by having better data about utilization.

In response to Representative McClure, Ms. Taylor-Brijklacich stated that the appropriate reserve amount is determined by looking at the claim costs and there is three months of claim dollars in the reserve fund. Ms. Taylor-Brijklacich presented a handout entitled "State of Arizona Self-Insurance Reserve Build-Up" (Attachment E).

Senator Cirillo clarified that while the project of self-insurance is ongoing, they are still looking at how to improve the provider networks in the State and more flexibility in the designs of the plans that are offered. This will save money and provide better service to rural Arizona.

Ms. Strickler explained that ADOA is looking at a three to five year process to improve the plan and networks. Their goal is to get financial control and to get control of the data.

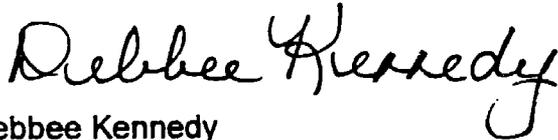
**Ms. Charlene Ledet, Special Assistant, State Relations, University of Arizona,** stated that the university supports ADOA's recommendation to delay the implementation of self-insurance for one year.

Senator Cirillo reiterated that the Committee will put together a draft report and include the salary recommendations by ADOA and the universities. It will be sent out for comments and suggestions before it is issued.

Mr. Nau thanked the chairs for all of their hard work.

There being no further business, the meeting was adjourned at 11:40 a.m.

Respectfully submitted,



Debbie Kennedy  
Committee Secretary

(Tapes and attachments on file in the Secretary of the Senate's Office/Resource Center, Room 115.)